2013-2014 QUALIFIED ALLOCATION PLAN

STAFF REPORT

INTRODUCTION

The Low Income Housing Tax Credit (LIHTC) Program has been in place since the enactment of the Tax Reform Act of 1986, and in 2012 entered its 26th year producing and rehabilitating affordable housing. Over that period of time, the program has changed at both the federal level and the state level, with program requirements being added and modified on a regular basis. This has also become true in Michigan where, because of these regular updates to the QAP, new requirements and policies were layered onto existing program requirements. This resulted in a more complex process for users of the program, and in some cases, policies that were no longer necessary.

With all of these things in mind and 25 years of history to look back on, MSHDA determined a significant re-write and overhaul of the QAP was necessary for 2013-2014. In its undertaking of this task, MSHDA developed guiding principles to help ensure that the ultimate goal of improving the QAP could be achieved. The four guiding principles for the significant re-write of the QAP for 2013-2014 were: stakeholder involvement; simplicity; investor friendliness; and achievement of policy objectives. While not a comprehensive list, the remainder of this document is intended to outline the process and some of the more significant elements of the 2013-2014 QAP compared to where the document had previously been, and it also shows how the guiding principles were satisfied.

STAKEHOLDER INVOLVEMENT

MSHDA identified early on that a significant modification to the LIHTC program requirements such as this could not be done without the involvement of stakeholders. Accordingly, MSHDA began the process for developing the 2013-2014 QAP in August of 2011 with an Informational Hearing to obtain ideas and suggestions from the general public on what should be included in the 2013-2014 QAP. Since that time, MSHDA has held several interest group meetings, stakeholder meetings and focus groups, including a day-and-a-half summit focused solely on the QAP. These conversations allowed for more opportunities for stakeholder input than had ever been available in the past, and has resulted in a more transparent and involved QAP development process. It has also resulted in an improved, more user-friendly process for developers and investors using the LIHTC program in the Michigan.

SIMPLICITY

One of the primary objectives as identified by MSHDA and stakeholders was the need for simplification. Over the years, the program documents had become lengthy and cumbersome. With that in mind, MSHDA made a very serious effort to try to make things simpler. In addition to simplifying the process and some of the program requirements, the QAP for 2013-2014 is approximately 20% shorter than the previous version of the QAP. Below are some of the revisions that have contributed to the overall simplicity:

FUNDING ROUND AND ALLOCATION PROCESS MODIFICATIONS

ONE FUNDING ROUND

Throughout the history of the LIHTC program in Michigan, there have been multiple funding rounds per year. However, upon reviewing this approach and comparing it to what other states around the country are doing, MSHDA has determined that it will begin having only one funding round per year. However, in effort to accommodate applicants who may have prospective projects in their development pipelines, this concept will be introduced gradually. The Authority will hold two funding rounds for 2013 credit and then will shift to the one funding round approach for 2014 credit. The primary purpose of this approach is to allow the total annual credit to be allocated sooner, which should allow more deals to get started sooner, and create jobs sooner than would be accomplished utilizing one funding round. Additionally, this approach will also improve administrative efficiency related to the MSHDA review process.

ELIMINATION OF TARGET PERCENTAGES

In prior QAPs there were Target Percentages for Central Cities; Detroit, Hamtramck, Highland Park (DHHP); and Underserved Populations (Native American Housing and Affordable Assisted Living). In the 2013-2014 QAP, these Target Percentages have been eliminated. In addition to making the allocation process simpler for applicants by removing these priorities, MSHDA's analysis of prior rounds found that these Target Percentages made little, if any, impact on the projects that ultimately received an award. Essentially, these Target Percentages have not been driving allocations in recent rounds and therefore can be eliminated without substantial effect on the outcome of the allocation process.

PRE-APPLICATION STAGE

Applicants will be required to submit evidence of land control, to order a market study, to provide development team information, to indicate which Category they intend to apply under, and to submit their project self-score as a pre-application stage to determine acceptability. Those applications that are found acceptable, based on MSHDA's review of these items, would be invited to apply for the competitive funding round. The idea behind this would be that applicants would know far enough in advance of the competitive funding round whether or not they have an acceptable site and whether or not the basic information submitted and reviewed by MSHDA is acceptable. This should lead to better project sites competing in the funding round and also allow applicants to save money on the additional costs of putting together an application for a project that may not be able to move forward.

WAIVER PRE-APPROVAL PROCESS

While it is not anticipated that the Authority will grant many waivers to projects applying for LIHTC in a competitive funding round under the revised QAP, the Authority does recognize the need for flexibility in certain unique situations. Accordingly, the Authority has created a process to be used for any project requesting a waiver as part of a competitive funding round.

Applicants requesting a waiver must submit a detailed waiver request at least 30 days in advance of the funding rounds for 2013 credit and no later than the Pre-Application stage for the 2014 funding round. Authority staff will review all waiver requests received, and provide a timely response back to the applicant. Responses will be given well in advance of the funding rounds for 2013 credit and no later than 60 days in advance of the competitive funding round for 2014 credit.

REMOVAL OF 180-DAY COMMITMENT DEADLINE (AND 90-DAY FOLLOW-UP) DEADLINE

For many years, MSHDA has had a LIHTC Commitment deadline of either 120 or 180 days following the award of LIHTC. The purpose of this deadline was to enforce "Readiness to Proceed" or "Hard Equity" points that projects took in their application and also to track a project's progress. Currently, projects are taking much longer to close as lenders and equity providers are continuing to do more due diligence and imposing stricter requirements on owners as part of the investor's underwriting process. In practice, this means that many projects, particularly those using HUD or USDA RD financing, cannot close within the currently applicable timeframes. Additionally, there are no longer "Readiness to Proceed" criteria contained within the scoring. In that context, the LIHTC Commitment deadline has been eliminated.

Post-award processing of applications in this fashion aligns with what many (if not most) other states are doing and allows for a simpler process for owners. Additionally, MSHDA will still ensure that all of a project's financing is in place and that a project is progressing forward, by reviewing the project at the federally-required 10% Certification deadline (1 year following award) and by continuing to require the development to submit progress reports.

ENTIRE APPLICATION IN EXCEL

In an effort to make completing and submitting an application easier for applicants, many of the application materials will now be in an Excel format that will allow for automated calculations and easy transfer of information both within and between project applications.

INVESTOR FRIENDLINESS

Critical to making the LIHTC program work is the involvement of investors who are willing to invest in the developments receiving an award of credit. If Michigan's QAP and the projects that receive an award as a result of it are not attractive to investors, then projects are likely to receive less favorable investment terms or to receive no equity investment at all. With that in mind, the following provisions were taken into account when developing the 2013-2014 QAP:

ELIMINATION OF 10% PERMANENT SUPPORTIVE HOUSING REQUIREMENT FOR ALL DEALS

In an effort to simplify the allocation and application process, and address investor concerns with risk and future service funding, the previous requirement that all 9% LIHTC family deals reserve 10% of their units for Permanent Supportive Housing (PSH) has been removed. However, MSHDA recognizes that a need exists for this type of housing and, therefore, will continue to make Project-Based Vouchers available to projects that agree to reserve a certain portion of the units for Permanent Supportive Housing. Additionally, applicants choosing to develop this type of "deconcentrated" supportive housing may now apply under the PSH Category as developments designating as few as 25% of their units as PSH are now eligible to compete in the PSH Category (for more on this, please see "Permanent Supportive Housing Category Modifications" below).

FINANCIAL CAPACITY OF SPONSOR

For many years, MSHDA has evaluated the financial capacity of the sponsors based on a net worth analysis. When focusing the review on net worth, many non-liquid assets are considered in the analysis such as property owned. In an effort to more appropriately conduct the financial capacity analysis, to more closely align with what equity providers are doing, and to simplify the process, this review will now be based on a sponsor's liquidity. A sponsor will need to have net liquid assets greater than or equal to 3% of the proposed permanent mortgages on all of the projects the sponsor currently has in the development process (i.e. following award and through placement in service date).

MODIFIED 130% BASIS BOOST CRITERIA TO FOCUS ON MORE POLICY-RELATED ITEMS

In prior years, the 30% basis boost was applied very liberally when the market was tougher and prices were lower, so that deals could get done, which was necessary at that time. However, now that the equity markets have rebounded somewhat, MSHDA re-evaluated what projects should get the basis boost of up to 30%. The projects that would now qualify are: PSH projects, Central Cities projects, Historic Rehab projects, projects scoring the full 10 green points (15% boost), projects setting aside at least 10% of their units for 30% AMI tenants, projects qualifying for the rural set-aside, and Strategic Initiative Category projects.

Additionally, a provision was added to assist in the event Congress does not extend the fixed 9% rate that projects are currently able to receive as long as they place in service prior to December 30, 2013. Should this fixed rate not be extended, the QAP would allow all projects to automatically qualify for a basis boost of up to 15% if needed for financial feasibility - the approximate amount needed to make up the difference between the fixed 9% rate and the monthly floating rate.

OWNER EXPERIENCE POINTS MODIFICATIONS

In prior years, owner experience was evaluated simply based on the number of previous projects that were completed, without much regard for the financial performance of those developments. The 2013-2014 QAP modifies this approach. Owners would now receive points based on the number of projects they have successfully completed, that are performing financially according to their lender and investor obligations. The idea behind this is that developers would get consideration not only for the amount of projects they have done, but also for the financial performance of prior projects.

ACHEIVEMENT OF POLICY OBJECTIVES

The primary purpose of the LIHTC program is to provide appropriate affordable housing for some of our neediest citizens, while also spurring economic development within our communities. Because of this, the final objective of the development of the Qualified Allocation Plan was to ensure that policy objectives are being met. In that context, the following items were incorporated in the QAP and/or its related documents:

CREATION OF A STRATEGIC INITIATIVE CATEGORY

There may be extraordinary circumstances where the evaluation of an application by the standard review process outlined in the QAP does not fully take into consideration the contribution that a development would make to the state's overall economic and community development strategy. These situations may include, but are not limited to, applications that demonstrate transformative neighborhood revitalization, and/or unique financial funding and leveraging opportunities, and/or the promotion of significant job growth in proximity to such housing. A Strategic Investment Category, totaling up to 10% of the total credit ceiling, has been created as an attempt to address these circumstances. If there are no qualifying projects for this Category, the credit will be used in the general funding round.

COST CONTAINMENT

One of the major areas of focus for the development of the 2013-2014 QAP, as identified by MSHDA and its partners, is the concept of cost containment and being able to use the limited 9% LIHTC resource efficiently. This issue is critical not only to the number of projects we are able to award, but also to the types of projects that will be developed in the state using the LIHTC program. This is a significant issue not only in the state of Michigan, but nationally.

In that vein, MSHDA convened a workgroup to focus solely on this issue. The result of that workgroup is a cost containment scoring model now included in the allocation process which awards points to projects by project-type – Preservation, New Construction, or Adaptive Reuse/Historic Rehab – based on its total development cost per-square-foot. To receive points, a project’s costs are compared to cost data on the last 5 years of LIHTC projects. Projects with costs less than the benchmark may receive positive points, while those with costs greater than the benchmark may receive negative points.

PERMANENT SUPPORTIVE HOUSING CATEGORY MODIFICATIONS

In prior years, the Permanent Supportive Housing (PSH) Category (and even the 10% PSH requirement) focused heavily on the number of units made available to PSH tenants. The 2013-2014 QAP changes this approach to focus more on the needs of the tenants and the services being provided rather than the number of PSH tenants in a development. Prioritization will be given to developments that "deeply target" to the needs of the tenants and that best align the services with these needs. Additionally, to qualify for this Category, a project will now only be required to set aside 25% of its units for PSH.

REVISED CRITERIA FOR LOCATION-BASED POINTS

In lieu of the complex location-based scoring that previous QAPs contained, including factors such as homelessness, unemployment, unit age, etc., the revised location-based scoring methodology in the 2013-2014 QAP is focused on supply and demand by project type. Specifically, for Open Category projects, the analysis will focus on the supply and demand of 30%-60% AMI affordable units; for Preservation projects, the analysis will focus on supply and demand of less than 30% AMI affordable units, since there will typically be some amount of rental assistance present; and for the PSH Category the analysis will focus only on the demand of less than 30% AMI affordable since there is limited supply.

ADDITIONAL SCORING ITEMS TO HELP RURAL AREAS

Rural areas are some of the neediest areas of the state and at the same time, these areas provide some unique challenges that projects located in larger communities may not face when assembling an application. Therefore, some additional and/or modified criteria were created to help address some of the issues that projects located in rural areas face and to create more of a competitive balance in the allocation process.

POINTS FOR LOCKING-IN THE PROPERTY TAXES

Rural communities, like many other communities across the state, are financially distressed. Asking a rural community's governing body to provide a tax break to a development through a Payment in Lieu of Taxes (PILOT) based on a low percentage of shelter rents related to a project, when it may be one of only a few apartment developments in town (or even the only one), is a difficult objective for a project sponsor or developer to achieve. Therefore, some points were added for projects where the municipality has at least agreed to fix the taxes at the amount currently being paid. While there will not be as many points for obtaining a fixed rate as there will be for obtaining a PILOT based on a percentage of shelter rents, there is still some benefit to a project being able to get its taxes locked, so some points are warranted.

POINTS FOR COMMUNITY SUPPORT IN LIEU OF COMMUNITY REVITALIZATION PLAN

Many smaller or rural communities do not have formal Community Revitalization Plans in place, but that does not necessarily mean that the community does not support the project or that the project is not meeting the same objectives for the community. It may just mean the community has not formally adopted a plan. Accordingly, in lieu of demonstrating that a project contributes to a Community Revitalization Plan, projects may receive points if they are able to have a resolution passed by the municipality indicating that a project will contribute to the community in the same way it would as if there were a plan in place.

POINTS FOR USDA RD SECTION 515 PROJECTS

In rural communities, there are many existing Section 515 projects, most of which have some portion of rental assistance, that are tired and in need of significant rehabilitation to preserve the subsidy. Further, in some instances, the developments may be one of the few (if not the only) affordable housing opportunities in some of these communities. Because of this, additional points were added to the scoring to put more emphasis on these deals.

BARRIER FREE SCORING CRITERIA

Several stakeholders have indicated the need for the inclusion of barrier free units as part of developments to help address a lack of these units in the market, and to help with integration among tenant-types. The competitive scoring now makes points available for projects that incorporate barrier-free design, or the ability for the units to be adaptable to barrier-free, into at least 10% of the total units.

MODIFICATION TO CALCULATION OF ACQUISITION PORTION OF DEVELOPER FEE

In the prior QAP, for acquisition/rehabilitation projects, a portion of the developer fee was calculated based on 15% of the acquisition costs of the property. This portion of the developer would ultimately be added to and counted towards a developer's total allowable fee. However, upon reviewing what many other states are doing, industry best practices, and some of the projects that have been submitted recently, this percentage of acquisition costs that can be counted toward the allowable developer fee was changed to 10% of the acquisition. Further, this will allow the limited 9% LIHTC resource to go a little bit further.

PROXIMITY TO TRANSPORTATION

Amenities are critical to the success of any project, one of which is the availability of public transportation. Residents like to live where they have the ability to use a variety of transportation means. The Scoring Criteria now makes points available to developments that are located within 1/10 of a mile of public transportation or that have the ability to make some other form of regularly scheduled transportation available to the tenants.

NONPROFIT OWNERSHIP

Several stakeholders have expressed concern over the ability to create for-profit/non-profit partnerships due to the previous requirement that the nonprofit had to have at least a 51% General Partner/Managing Member interest in order to receive the points. This created little incentive for a for-profit developer to want to enter into a partnership with a nonprofit, and also resulted in a larger "experience gap" between many of the for-profit developers and their nonprofit counterparts. In an attempt to try to create more viable partnerships between for-profits and nonprofits, different levels of points have been added to allow some additional points to be received if a nonprofit has an ownership interest above 20%, all the way up to 50% or greater.

ELIMINATION OF POINTS FOR 4% PILOT RATE

In the prior version of the QAP there were points available for projects that could obtain a PILOT with a rate of 4% or lower. While obtaining a 4% PILOT is good for a project, it also can create additional financial stress for many of Michigan's communities that are currently financially distressed. Additionally, if a project is financially feasible at a rate greater than 4%, should it be penalized when it may not need the lower PILOT rate? It is in that context that the points for having a PILOT of 4% or less have been removed.

REMOVAL OF FEDERAL, STATE, LOCAL FINANCING

The purpose of having points available for projects using other Federal, State, or Local sources of financing was to provide some incentive for leveraging other resources, which should ultimately reduce the amount of LIHTC a project would need. Additionally, these sources are generally received at more favorable terms, whose benefits can be passed on to the tenant in the form of lower rent. In practice, however, a project will usually determine the maximum amount of LIHTC it can qualify for and then determine how much gap financing (normally federal, state, or local source) it would need for the project to be financially viable. Often, this means that the amount of credit projects are requesting isn't necessarily due to leveraging of the other sources in the deal; it more likely means that projects may be looking for more gap funding sources than necessary so that they could receive the points.

RE-EVALUATION OF SCORING

Stakeholders expressed, and MSHDA agrees, that the QAP should allow for a level playing field among application submissions. The entire Scoring Criteria document was reviewed to try to ensure a competitive balance among project types and across Categories. Additionally, the entire document was reviewed to determine the relevancy of the some of the scoring items previously contained in the Scoring Criteria. This means that in many cases point values were adjusted or scoring items were removed to try to accomplish both of these goals.